SHENCOURT SDN BHD

v.

PERUMAHAN NCK SDN BHD

HIGH COURT MALAYA, KUALA LUMPUR
RAMLY ALI J
[ORIGINATING SUMMONS NO: D5-24-185-2005]
27 OCTOBER 2005

COMPANY LAW: *Winding up - Leave to continue suit against company ordered to be wound up - Criteria for granting leave - Companies Act 1965, s. 263*

COMPANY LAW: *Winding up - Proof of debts - Whether lodging proof of debt a mandatory statutory process*

COMPANY LAW: *Winding up - Distribution of company's property - Court's duty to ensure all assets are distributed pari passu among unsecured creditors - Court's duty to ensure no undue preference*

The plaintiff was a development company engaged in a development project, of which the defendant was the main contractor. The defendant commenced an action against the plaintiff *vide* Civil Suit No: S5-22-77-2004 pursuant to a settlement agreement in regard to the amount of RM900,000. Consequent to the cessation of works by the defendant, the plaintiff appointed another new contractor to complete the remaining works left. Upon examining the works to be continued and completed the new contractor discovered serious latent defects which needed to be rectified as they were wrongly carried out by the defendant. The estimated costs of rectifying these latent defects was about RM17,898,000 and the plaintiff counter claimed this sum against the defendant's claims under the settlement agreement. After the defence and counter claim was filed by the plaintiff, the defendant was voluntarily wound up by their creditors. The plaintiff applied for leave pursuant to s. 263(1) of the Companies Act 1965 ("the Act") to proceed with their counter claim against the defendant in Civil Suit No: S5-22-77-2004.

Held (dismissing plaintiff's application with costs):

[1] Leave to proceed pursuant to s. 263(2) of the Act would only be granted when it is a question of expedience and convenience: (a) when the plaintiff's claim cannot be adequately dealt with in the winding up of the defendant's company; and (b) when the plaintiff is seeking a remedy which cannot be given in the winding up of the company. (p. 656 d-e)

[2] Lodging a proof of debt constitutes a mandatory statutory process for a creditor of a wound-up company. The institution and continuance of the plaintiff's counter claim in S5 suit or even the recovery of any judgment that will be obtained by the plaintiff against the defendant will operate to confer sort of an unfair priority or advantage and undue preference on behalf of the plaintiff over the other creditors of the defendant company including the secured creditors. This should not be condoned by the court. (pp. 656 h & 657 a)

[3] It is impractical and unnecessary to proceed with the plaintiff's counter claim in the S5 suit when the proof of debt process in the winding up of the defendant company served the very same purpose (*ie*, to determine whether the plaintiff's counter claim is a valid claim or not) more cheaply and expeditiously than a full blown trial. (p. 659 h-i)

[4] The plaintiff's counter claim was a purely speculative claim which most probably would not succeed. In authorizing proceedings, especially if they may or will involve some drain upon the assets of the company, the court must satisfy itself as to the probable success of the claim or counter claim. (p. 661 g)

[5] A judge in winding up proceedings is the custodian of the interests of every class affected by the liquidation. It is his duty to see that all assets of the company are brought into the winding up and distributed *pari passu* amongst unsecured creditors. In granting leave of this nature a judge must be satisfied it would not result in rendering an unnecessary heavy financial strain on the company which would gradually deplete or draw the assets and resources of the defendant company or ultimately will operate to confer sort of unfair priority or advantage and undue preference on the plaintiff over the other creditors of the defendant company, including the secured creditors. (pp. 661 h & 662 a-b)

Case(s) referred to:

Asean Security Paper Mills Sdn Bhd v. Provincial Insurance (Malaysia) Sdn Bhd [2000] 1 CLJ 759 HC ***(refd)***

Century Mercantile Co v. Auckland Provincial Fruitgrowers Society [1921] NZLR 272 ***(refd)***

Chatib Kari v. Mosbert Bhd [1984] 2 CLJ 30; [1984] 1 CLJ (Rep) 501 HC ***(refd)***

Maher v. Taylor & Ors [1983-1984] CLR 931 ***(refd)***

Mosbert Berhad (In Liquidation) v. Stella D'Cruz, [1985] 1 LNS 47 FC ***(refd)***

Ogilvie-Grant & Anor v. EAST Liquidator of Gordon Grant and Grant Pty Ltd [1982-1983] ACLR 669 ***(refd)***

Re Campall Sdn Bhd; Perdana Merchant Bankers Bhd (Applicant) [1997] 1 LNS 408 HC ***(refd)***

Legislation referred to:
Companies Act 1965, ss. 236(1)(e), (j), 263(1), (2), 264, 291, 292
Companies (Winding Up) Rules 1972, r. 39
Rules of High Court 1980, O. 14, O. 812

For the plaintiff - Wee Su Lin; M/s Yusuf Khan & Fong
For the defendant - Olivia CW Ho; M/s Paul Ong & Assoc

Reported by Amutha Suppayah

JUDGMENT

Ramly Ali J:
This is an application by the plaintiff for an order that the plaintiff be given leave pursuant to s. 263(1) of the Companies Act 1965 to proceed with their counter claim against the defendant in Kuala Lumpur High Court Civil Suit No: S5-22-77-2004 and the costs of the application to be borne and paid by the defendant to the plaintiff upon taxation thereof.

Brief Facts
The plaintiff is a development company engaged in the development project of a complex known as Galaxy Ampang, of which the defendant as main contractor was responsible for the building construction thereof, having taken over the contract from the previous contractor.

The matters relating to the works in question are contained in those documents known as the letter of intent dated 18 May 1996, the supplementary letter of award dated 29 August 1997 and a new letter of award dated 29 August 1997 and another letter of award dated 1 September 1999. The defendant's action in Kuala Lumpur High Court Civil Suit No: S5-22-77-2004 is pursuant to the settlement agreement dated 13 March 2001 *inter alia*, in regard to the amount of RM900,000 to be paid in cash and specific performance of the units of properties in the complex to be transferred to the defendant or his nominees or alternatively the sum of RM1,585,668 representing the value of the said units and RM156,443.30 representing the short-fall of the contra-value and rental for the tower crane amounting to RM365,000.

Vide settlement agreement dated 22 December 1999, the parties resolved to settle the payment of the works completed up till 22 December 1999 which was to be effected by monetary as well as contra-payment in the form of sale and purchase agreements in respect of contra-units in the complex.

Subsequently a second settlement agreement was entered into on 13 March 2001 (the final settlement agreement) which *inter alia* supercedes the aforesaid settlement agreement particularly in the mode of payment.

Consequent to the cessation of works by the defendant, as envisaged by the said final settlement agreement, the plaintiff appointed another new contractor to complete the remaining works left.

Upon examining the works to be continued and completed the new contractor discovered serious latent defects which so fundamental as to render it impossible to continue the works from where the defendant left them for the new contractor as these had to be rectified first and in certain instances to be redone, as they were wrongly carried out and completed contrary to specifications and basic requirements.

The estimated costs of rectifying these latent defects is about RM17,898,000 and is now made the subject of the plaintiff's counter claim against the defendant's claims under the final settlement agreement.

After the defence and counter claim was filed by the plaintiff, the defendant was voluntarily wound up by their creditors on 28 April 2004.

The defendant's defence to the plaintiff's counter claim is, *inter alia*, that the plaintiff's counter claim is baseless, frivolous and vexatious as it was made merely to delay and avoid the plaintiff's liability to the defendant.

Parties have filed their respective pleadings in the court and the plaintiff's appeal against the summary judgment obtained by the defendant in the said civil suit pursuant to O. 14 of the Rules of High Court 1980 was allowed by the court whilst the defendant's application for specific performance pursuant to O. 812 of the Rules of High Court 1980 was withdrawn by the defendant with no order as to costs. The matter is now fixed for case management.

Law Regarding Leave to Proceed

The plaintiff's application for leave to proceed with its counter claim against the defendant in the said civil suit is pursuant to s. 263(2) of the Companies Act 1965 which reads:

> After the commencement of the winding up no action or proceeding shall be proceeded with or commenced against the company except by leave of the court and subject to such terms as the court imposes.

In *Mosbert Berhad (In Liquidation) v. Stella D'Cruz,* [1985] 2 MLJ 446, Seah SCJ, delivering the judgment of the Supreme Court held at p. 447:

> In *re Cuthbert Lead Smelting Co. Ltd.* [1886] WN 84 it was held that if the applicant could obtain all the relief in the winding up leave would be refused. In short, the court will always give an application for leave if his claim cannot be dealt with adequately in the winding up or if the remedy he seeks cannot be given to him in a winding up proceedings.

In *Century Mercantile Co. v. Auckland Provincial Fruitgrowers Society* [1921] NZLR 272, the court stated that:

> The only material question to be considered is whether there are any circumstances which render it necessary that the action should be continued, or whether the claim of the plaintiff is not one which can be as easily dealt with in the winding up as in any other way.

In *Re Campall Sdn Bhd; Perdana Merchant Bankers Bhd (Applicant)* [1997] 3 MLJ 435, Abdul Malik Ishak J held at p. 458:

> It is apparent that the question posed here is fundamentally one of expedience and convenience (*Re Queensland Mercantile Agency Co*. [1888] 58 LT 878; *Steward v. Intercity Distributors Ltd.* [1960] NZLR 955; *Maker v. Taylor* [1984] 8 ACLR 931). The court will also examine the amount and seriousness of the claim, the degree of complexity of the legal and factual issues involved, and the stage which the proceedings have reached before deciding that leave should be given: *Ogilvie-Grant v. East* [1983] 1 ACLC 742.

The above authorities confirm that leave to proceed would only be granted when it is a question of expedience and convenience:

(a) when the plaintiff's claim cannot be adequately dealt with in winding up of the defendant's company; and

(b) when the plaintiff is seeking a remedy which cannot be given in the winding up of the defendant company.

In the present case, the plaintiff's counter' claim against the defendant is for the sum of RM17,898 million allegedly being rectification costs for defective works for the said project. This is a claim for damages for breach of contract. Damages and breach of contract involve simple and common issues of facts and laws. No specialized knowledge is needed to examine and discern whether the said counter-claim is *bona fide* or not. It is trite law as laid down in *Chatib bin Kari v. Mosbert Bhd*. [1984] 2 CLJ 30; [1984] 1 CLJ (Rep) 501 that "leave is almost invariably refused where the claim is in respect of what is no more then a simple contract debt which can be submitted to proof in the ordinary way...".

Lodging a proof of debt constitutes a mandatory statutory process for a creditor of a wound-up company like the defendant company in the present case. It is a statutory policy of ensuring that assets of the company are distributed rateably amongst all creditors so that none of them will gain advantage over the others. The Supreme Court in *Mosbert* case states that "... the primary object of winding up is the collection and distribution of the assets of the company *parri passu* amongst unsecured creditors after payment of preferential debts."

However, the institution and continuance of the plaintiff's counter claim in S5 suit or even the recovery of any judgment that will be obtained by the plaintiff against the defendant will operate to confer sort of an unfair priority or advantage and undue preference on behalf of the plaintiff over the other creditors of the defendant company including the secured creditors. This should not be condoned by this court.

The plaintiff is not restrained or impeded in any way from lodging a proof of debt with the liquidators of the defendant's company. The plaintiff alleged that the liquidators of the defendant's company 'have already prejudged the matter and would definitely dismiss the plaintiff's proof of debt.' How could the plaintiff makes such an allegation when in actual fact the plaintiff has never even taken any step of lodging in the winding up proof of debt or forwarded any supporting evidence of the plaintiff's counter claim for the consideration of the defendant's liquidators?. Such averment is baseless and without merit considering that the liquidators are independent and unpartial officers of the court and in the present case, have more than 20 years of experience under their belts.

The liquidators may appoint an advocate and solicitors to assist them in their duties or even a special manager to do all such things as are necessary for winding up the affairs of the company and distributing its assets including analyzing the merits of the plaintiff's counter claim, (see: s. 236(1)(e) and (j) of the Companies Act 1965 and r. 39, of the Companies (Winding Up) Rules 1972). Hence, the plaintiff's allegation of the defendant's liquidators being bias or incompetent to deal with the plaintiff's counter claim is totally baseless and unjustified.

In any event should the plaintiff be unhappy with any decision of the defendant's liquidators made after the lodging and consideration of the proof of debt, the plaintiff still has recourse to appeal to the high court against the aforesaid decision.

The plaintiff is not deprived of any legal right nor prejudiced in any way.

A *fortiori* the plaintiff has only filed its counter claim recently and the said counter claim is only at the stage of case management. What prejudice would the plaintiff suffer if the plaintiff just proceeds with the lodging of proof of debt instead of continuing with its counter claim?

The above is in line with the decision of Supreme Court, in *Ogilvie-Grant & Anor v. EAST Liquidator of Gordon Grant and Grant Pty. Ltd.* [1982-1983] ACLR 669 that:

> As a matter of history, a winding up by the court was and remains today an administration conducted by the court ... What is substituted for litigation in the ordinary form is a procedure by which a claimant lodges a verified proof of

> debt with the liquidator, who admits or rejects it wholly or in part, and from whom an appeal lies to a judge, who determines the appeal *de novo* primarily on affidavit material ... There can be no doubt that ordinarily such a procedure is, and is designed to be, much more expeditious and less expensive than ordinary proceedings by way of action ... it seems to me to be quite wrong at this juncture to slow the liquidation to the pace of an action under the control of others, in which the pleadings have not yet even closed ... It follows that the injustice to the appellants of being involved ... is more than outweighed by the additional delay and expense that will ensue of their claim is not dealt with by the procedure prescribed for proving claims in winding up. The appellants have therefore failed to demonstrate the advantages of permitting their claim to be established by third party proceedings in the action rather than by the statutory process of proof of debt ... .

Conversely to allow the plaintiff to proceed with its counter claim in the S5 suit would be time-consuming and involves substantial costs being expended on the part of the defendant company.

Recently the plaintiff has also applied for security for costs against the defendant company in the S5 suit.

In the long run the trial of the plaintiff's counter claim and hearings of various other interlocutory applications filed or may be filed by the plaintiff against the defendant company would render an unnecessary heavy financial strain on the defendant and would gradually deplete or drain the assets and resources of the defendant company.

This goes contrary to the purpose and principle of winding up when assets of the defendant company ought to have been preserved for fair distribution amongst the creditors and not to be exhausted unnecessarily. The interest of the other creditors and the public ought to be protected by the court.

The Supreme Court *Maher v. Taylor & Ors.* [1983-1984] CLR 931 has enunciated that:

> ... The plaintiff applied for leave to continue defamation proceedings against a corporate defendant (the company) which was in liquidation ... The winding up was a creditors' voluntary winding up and had been commenced after the defamation action was brought ... the court should not give its imprimatur to fruitless proceedings which can only involve a waste of public time and money ... where ... prejudice - procedural or substantive - will result from the proceedings to the other creditors who have interests in the winding up., there is a good reason for refusing leave when there is no prospect of surplus assets in the company and no question of insurance ... the rights of the company's creditors may still be gravely affected by a continuation of the proceedings against the

company. If the proceedings are continued, the liquidator must elect either to expend the company's assets in defending them or to allow the plaintiff's claim to go by default... .

The court in *Chatib bin Kari v. Mosbert Bhd.* [1984] 2 CLJ 30; [1984] 1 CLJ (Rep) 501 has also said that:

Why is leave of the court necessary? ... for the purpose of preserving the limited assets of the company ... in the best way for distribution among all the persons who have claims upon them. There being only a small fund or a limited fund to be divided among a great number of persons, it would be monstrous that one or more of them should be harassing the company with actions and incurring costs which would increase the claims against the company and diminish the assets which ought to be divided among all the creditors... .

The Supreme Court, *Mosbert Berhad (In Liquidation) v. Stella D'Cruz* [1985] 1 LNS 47 states that:

... the purpose of the statutory provision is to ensure that all claims against the company in liquidation which can be determined by the cheap and summary procedure available in a winding up are not made the subject of expensive litigation. The provision is designed to prevent unnecessary multiplicity of suits which may result in dissipating the assets of the company... .

If the plaintiff is given leave to proceed with its counter claim in S5 suit, the scenario would be like this:

(a) after a prolonged trial (the duration of which may even exceed a few years) the plaintiff's counter claim would be determined.

(b) in the event the plaintiff's counter claim is allowed, the plaintiff would still have to lodge proof of debt of any judgment obtained for its counter claim.

(c) pursuant to ss. 264, 291 and 292 of the Companies Act 1965 the plaintiff's counter claim (subject to proof of debt being lodged) would still be an unsecured debt and paid in accordance with the principle of pari passu after the payment of preferential and secured debts.

In short, the adjudication of the plaintiff's counter claim in S5 suit would still result in the plaintiff's counter claim being reverted to proof of debt at the end of the day. Therefore, where is the necessity or expediency for the plaintiff's application for leave to proceed with its counter claim herein?

It is impractical and unnecessary to proceed with the plaintiff's counter claim in the S5 suit when the proof of debt process in the winding up of the defendant company serves the very same purpose (ie, to determine whether the plaintiffs counter claim is a valid claim or not) and is in fact much more cheaper and expeditious than the toils and hassle of a full blown trial.

It is also obvious from the plaintiff's non-action (by not lodging any proof of debt) or action for that matter (in filing the plaintiff's counter claim against the defendant's original claim) that the plaintiff's counter claim is drummed up to thwart and delay the defendant's original claim as well as to disrupt and delay the winding process of the defendant company which would only result in the perpetration of injustice.

The plaintiff's application for leave is evidently a fruitless proceeding and a waste of time and costs of both the defendant company and this court.

The Plaintiff Is Seeking A Remedy Which Can Be Given In The Winding Up Of The Defendant Company

The plaintiff is essentially seeking a determination of its counter claim. The said determination can easily be done through the lodging of proof of debt with the liquidators of the defendant company. It is not necessary to have the same adjudicated by way of civil suit.

In the original claim, the defendant claims for the sum of RM2.8 million agreed to be paid by the plaintiff to the defendant pursuant to the settlement agreement.

Racital 6 to the settlement agreement read together with cl. 1 and cl. 2 of the same agreement state that:

> ... The parties hereto hereby mutually agree to irrevocably rescind the relevant clause of the First Settlement Agreement ... And has resolved by the terms hereof to settle all pending or outstanding unresolved matters between the parties hereto including all progress work done from 1 September 1999 to 31 May 2000 ... by entering into this Agreement intended to be a final settlement agreement between the parties hereto and intended to supercede all provisions of the Main Contract, the Supplementary Contract, the Current Contract and the First Settlement Agreement' ... hereinafter be collective called 'the Collective Agreement' ... In consideration of the mutual resolution of all pending and outstanding unresolved dispute or breaches of whatever kind and nature and howsoever occurred between the parties hereto in relation to the Work on the Complex and/or pursuant to the Collective Agreement, the parties hereto have agreed to irrevocably terminate the Collective Agreement absolutely ... neither party shall be entitled to rescind resile and/or retract from the terms herein stipulated and on whatever reason/s ... As final settlement of all pending claims due to the Contractor from the Collective Agreement, Shencourt undertake agree and covenant to pay to the Contractor a sum of ... RM2,800,000 ... as full and final settlement of the Work completed on the Complex ... pursuant to the Collective Agreement ... .

In accordance with the express terms of the settlement agreement as adumbrated above, it is *prima facie* evident that the plaintiff is not entitled to make any further claim including the plaintiff's counter claim herein which is purportedly based on latent defects in relation to works which had been fully completed by the defendant and agreed to be fully settled by the plaintiff under the settlement agreement.

In light of the express terms of the settlement agreement, the sole question to be determined is only a question of liability ie, whether the defendant is liable for the latent defects alleged by the plaintiff. Such question of liability hinges on the construction of the effects and intention of the settlement agreement.

This question has already been raised by the plaintiff itself *via* its statement of defence filed against the defendant's original claim wherein the plaintiff has alleged particularly in para. 8 that:

> ... Selanjutnya, defendan menyatakan bahawa tuntutan plaintiff telah disalah tanggap oleh plaintif dan perjanjian penyelesaian bertarikh 13 March 2001 adalah terbatal ... .

From the statement of defence filed by the plaintiff in the original claim, the plaintiff is already asking the court to grant a declaration that the settlement agreement is null and void.

Therefore, the plaintiff's allegation that the plaintiff's counter claim must proceed because the winding up court could not grant any relief in the form of a declaratory order cannot stand at all when the plaintiff's prayer for declaration can be adequately dealt within the original claim. There is no need for ventilation of the said issue in the plaintiff's counter claim anymore.

The plaintiff's counter claim is based on estimated costs. It is purely a speculative claim which most probably would not succeed. In authorizing proceedings, especially if they may or will involve some drain upon the assets of the company, the court must satisfy itself as to the probable success of the claim or counter claim, (see: *Asean Security Paper Mills Sdn. Bhd. v. Provincial Insurance (Malaysia) Sdn. Bhd.* [2000] 1 CLJ 759).

Conclusion

A judge in winding up proceedings is the custodian of the interests of every class affected by the liquidation. It is his duty to see that all assets of the company are brought into the winding up and distributed *parri passu* amongst unsecured creditors. A judge plays an important role in winding up of a company. After the winding up order was made by him, liquidators are

appointed and supervised by him until the winding up process is over. It is an administration conducted by the court. In granting leave of this nature a judge must be satisfied it would not result in rendering an unnecessary heavy financial strain on the company which would gradually deplete or draw the assets and resources of the defendant company or ultimately will operate to confer sort of unfair priority or advantage and undue preference on the plaintiff over the other creditors of the defendant company, including the secured creditors.

In the present case, it is not a proper case to grant leave as requested by the plaintiff. The plaintiff's claim against the defendant company can be adequately dealt with in the winding up of the defendant company by lodging its proof of debts. On that premise, the court dismissed the plaintiffs application with costs.